The Conceptual Framework Related to the Enterprise's Performances

Ghintuiala Alexandrina

Danubius University of Galati, Economic Sciences Faculty,
alexandrinaghintuiala@univ-danubius.ro

Abstract: The performance is characteristic to a state of competitiveness of the enterprise which must not be mistaken for the indicators which describe it. From a quantitative point of view, the financial performance versus the result is defined from the perspective of the enterprise's profitability. It is imposed the transition from the evaluation at historical prices to the evaluation at the correct value, from the abandonment of the concept of the past and present period's result to the concept of performance respectively, which gives the future perspective of the enterprise. Regarding the predictive capacity of the financial performance indicators, it can be noted that the exploitation's result, the treasury flow and the added value serve the future treasury flows.

1. Dimensions in defining the concept of financial performance

Performance is a state of competitiveness of the entity, which ensures a durable presence of the said entity on its markets by achieving its strategic objectives. How can this performance be achieved? "by engaging the enterprise in the process of lasting development, which implies creating value for the shareholders, satisfying the customers and the employees, respecting the natural and the social environment."[1]

The term "performance" is used with a certain degree of imprecision nowadays. In spite of the fact that it is abundantly used with multiple meanings, the term "performance" is rarely defined, even in works where is considered the main study subject. To define performance you must start from the notion of the enterprise's performance itself, from the cause of its economic recognition, from the performance's measurement and from the way in which it is presented in financial situations.

It is generally accepted that performance[2] represents a special accomplishment in a domain of activity/field. This definition leads to the conclusion that "the performance is not an observation, it is accomplished or it is built." (Bourguignon, 1995).

The enterprise's performance is addressed more to the enterprise's possibility to make profit. From here results the potential size of the resources that the enterprise will have and control in the future[3].

[1] Jianu Iulia, "The Evaluation, The Layout And The Analysis Of The Enterprise's Performance. An Approach From The Perspective Of The International Standards Of Financial Reporting", CECCAR Ph. H., Bucuresti, 2007, p.123.
[2] DEX, Univers Enciclopedic Ph. H., Bucuresti, 1996.

Jean-Claude Scheid reminds us that until the first half of the XXth century, accounting had been used more for an activity named "inventory" instead of "balance of accounts" or "balance sheet", rather than for computing the result. The investor is looking for financial security and the balance sheet will emerge to bring it forth, to the detriment of the profitability's analysis but also of the economic analysis in relation to fluctuation.[4]

The French conception of the result is in accordance with the well known priority of the balance of accounts.

B. Colasse emphasizes that: "taking into account the regular and normal definitions of the notions of income and expenses, the result is strictly of a patrimonial nature and corresponds to the income the enterprise procures to its owners."[5]

Because of the intensity of the relations between accounting and taxation, is isn't surprising at all that we encounter the approach from the balance of accounts point of view in the definition which is given by the General Code of Taxes from France for the net result: "…constituted by the difference between the net assets' values at the termination and those corresponding with the start of the exercise".[6]

Going by a certain conception, the results' account becomes, in a manner of speaking, an annexation of the balance of accounts, which explains the fluctuation of the intrinsic capital, exclusively new contributions and sharing or distributions.

It must not be overlooked the subjectivity that accompanies the concept of result and which causes are to be found in the perspectives of the different categories of users on the result and in politics and accounting options.

If the result were to be judged from the perspective of the enterprise's owners, it would be represented by the difference between income and expenses, including financial and staff expenses.

As soon as the value of an enterprise or rather of its shares is not computed anymore as the sum of the values of the patrimonial elements, but perceived as its capacity to generate economic advantages, the balance of accounts loses importance when confronted with the account of profit and loss, which translates better this capability. Going by such an approach, the result does not express a fluctuation of the patrimony (gain or loss) anymore, but becomes an indicator for performance.

2. The enterprise's financial performance starting from financial situations

The performance must not be mistaken for the indicators which describe it, "performance is characteristic for a state of competitiveness of the enterprise, which ensures the enterprise's long-term presence on the market".[7]

---

[3]Emil Horomnea, "The Scientific Basis Of Accounting. Doctrine. Concepts. Lexicon", Tipo Moldova Ph. H., Iasi, 2008, p. 231.

[4] Jean Claude Scheid, "La varieté des notions de résultat pour intreprinse", Actes du 4-é Congres de l'AFC, 1984, p. 89

[5] Bernard Colasse, "Comptabilité générale", 9th Edition, Economica Ph. H., Paris, 2005

[6] Judith Saghroun, Claude Simon, "Bilan ou compte de resultat Faut-il choisir?", Congrés AFC, Nantes, 1998

[7] Jianu Iulia, "The Evaluation, The Layout And The Analysis Of The Enterprise's Performance. An Approach From The Perspective Of The International Standards Of Financial Reporting", CECCAR Ph. H., Bucuresti, 2007, p. 54

Information concerning the performance of an entity, especially its profitability is necessary for the evaluation of the potential modifications of the economic resources which could be controlled by the entity in the future. From this point of view, the information about the performance's variability is important. Information about performance is instrumental in anticipating the entity's capacity to generate cash flows with the help of the available resources. Information about performance is also useful in formulating reasoning about the efficiency with which the entity could utilize new resources.

From the quantitative point of view, the financial performance versus the result is defined from the perspective of the enterprise's profitability. The equation used in this case has the following form:

The result of the exercise= The exercise's income- The exercise's expenses

Providing that the result is defined as the difference between income and expenses, the last two components being considered as structures of the owner's equity. It follows that the result can also be defined from the perspective of the owner's equity fluctuation, the equation created for this purpose having the following form:

Result of the exercise N= The owner's equity of exercise N – The owner's equity of the exercise N-1 ± The contribution to the capital (contribution/reimbursement) of the owner during the exercise N ± Other growth/diminution of the capital other than that of the exercise's N.

The accounting result has developed in time [8]. In economies similar to that of the U.R.S.S. from Stalin's period, the accounting result was represented by the difference between sales, on one hand, and the assembly of consumption and staff's emolument, on the other hand. Interest rates and taxes were not perceived as expense but dispensation of the result, which was justified by the fact that the majority of enterprises was the property of the state. In Yugoslavia's economy from Tito's period, which was of the self-administrative type, the accounting result of the enterprise was represented by the difference between sales, on one hand, and the sum of consumption, interest rates and taxes on the other. The emolument of the staff was not considered as being an expense because the owners of the enterprise were associated producers.

Between the 13th century ant the 19th century, static accounting has been progressively elaborated. According to the static accounting, an enterprise could not distribute the results or share losses until the expiry of the firm's activity object, the expiry of the contract or the disappearance of one of the associates. To compute the net assets of a given period of time, the sum of the assets generated by their stocktaking, supposing fictitiously that they were sold separately, from which were then deducted debts contracted by the entrepreneur, are compared to the net assets of the preceding period of time. According to this type of reasoning, the enterprise was found in the fictitious situation of being wound up, although it continues to exist.

Dynamic accounting, which is as old as the static one and has as its objective the permanent measurement, at small time intervals, of the enterprise's efficiency and which is represented in principal by the owner's equity profitability, namely the ratio between the net result which is rightfully given to the owners of the enterprise and owner's equity which belongs to these owners. The result is determined by the difference between income and expenses. In dynamic accounting, with the period's income from selling the merchandise and finished goods, is included the potential income from the stocked production and from the present production, representing the potential selling price of these

[8] James Richard, "Comptabilité et pratique comptable" Dalloz PH. H., Paris, 1996.

stocks. The use of the working capital is known as expenses and is disguised as depreciation, raw materials used, services rendered, emolument of the staff, etc.

Those who promote the dynamic conception, have asked themselves about the moment in which the result should be acknowledged: the time of the order, of the production, of the billing or of the payment; however, these questions have not been asked by those who promote the static accounting because according to their conception, all the assets were achieved fictitiously..

In conformity with the principle of prudence, substituting the cost for the selling price can be made at the time of payment (maximum prudence), at the delivery time (medium prudence) or at the end of production time (minimum prudence). In practice, profit is acknowledged at the time of delivery. Irrespective of the time when the profit is acknowledged, the enterprise's result at the end of the exploitation period is the same.

Between the promoters of the purely static conception(the evaluation of the assets at the potential selling price) and the promoters of the dynamic conception (the evaluation of the assets unrealized at the cost) exists a third system in which the unrealized assets are evaluated at cost when the potential value on the market is superior to the cost and the market price when it isn't. However, the inclusion of potential losses and the exclusion of potential profits hamper the rational evaluation of the result.

To project a real image of the way in which the result is influenced by the fluctuation of value generated by the variation of the correct values, these must be registered directly in the unique situation of the performance, aspect which can be explained by the fact that the surpluses of value generated by the rise of prices does not represent profit; they must be presented in an account related to the adaptation to inflation which must not affect the performance of the enterprise – an owner's equity account.

According to the presentation made it can be observed that none of the two accounting types, static and dynamic, can render the general value of the enterprise. This occurs because dynamic accounting evaluates assets at the minimum between cost and market value not taking into consideration the potential value surpluses, which often prove to be reliable and in static accounting because, although assets are presented at market value, it can be considered a forced sale of assets separately/individually, and not globally and most intangible assets are not taken into consideration.

All these drawbacks could be overcome by adopting the evaluation at correct value for all the elements- assets and liabilities.

However, it remains unsolved the problem of finding adequate methods for the evaluation of the goodwill, internally product of employee's knowledge, etc.

An alternative to the evaluation at correct value is actuarial accounting which presents the general value of an enterprise and which has as its target the comparison between the updated values of an enterprise at different moments in time. When using the updated cash flows which the invested capital permits to be generated in the future, exist many questions regarding the reliability of such an accounting system, especially related to the method of calculation of cash flows and the update factor.

Today the accounting result does not appear anymore as an appropriate variable in informing financial markets about the value of the firm and its activity; the final result becoming the adequate indicator which informs about the enterprise's performance, because it takes into account not only the past and present results, but also the possibility of obtaining a favorable result in the future. In order to judge correctly the performance of an enterprise starting with the financial situations, it is necessary for the accounting politics of the enterprise to be well controlled.

Different methods which have different results do not affect the performance of the enterprise, but the qualitative aspect of the accounting information regarding the ability to compare.

The transition from the accounting result to the global result is considered a transition from the evaluation in historic costs to the correct/just value, respectively from the abandonment of the concept of result of the past and present period to the concept of performance which renders the future perspective of the enterprise.

The General IASB and LAS 1 Framework "The layout of the financial situations" estimates correctly that the profit-and-loss account does not highlight completely the performance of the enterprise.

It must not be overlooked the manner in which the elements that are specific for performance are classified, regrouped and presented so that they serve the financial situations' objectives well. Presently, IASB solicits the creation of a statement of the global result in coordination with the layout of a situation which should reflect all variations of the owner's equity. But as the objective of the two statements is so different, IASB should not ask enterprises to choose. The statement of the global's result, named by IASB "the statement of income and losses" is a statement which reflects the global performance of the enterprise, while the variation of the owner's equity statement, as the name suggests, is just a simple layout of the owner's equity modifications, comprehensive enough to present adequate information.

The calculation of the global result, which reflects the financial performance of the enterprise, in the FASB's vision is the following:

The global result= Return of the year(the result of the exercise)± Incomes and losses taken directly into account in the owner's equity ± The effect of modifications in accounting politics and fundamental errors

As it can be understood from The General IASB Framework, the adjustments for maintaining the owner's equity consist of plusvalues and minusvalues from the reevaluation or adjustment of the value of assets and liabilities which determines growth or diminution of the owner's equity. Although growth or diminution are in correspondence with the definition of income and expenses, they are not included in the profit-and-loss account on the basis of some concepts linked to maintaining the capital's level. However, they are included in the owner's equity, as adjustments made to maintain the capital's level or as reevaluation reserves. In fact, all the elements corresponding to the definition of income and expenses should be included in an unique statement of performance, to evade the risk of considering a part of the significant elements, as are those from the profit-and-loss account, and other insignificant elements, as is the case of income and losses accounted directly in the owner's equity. The double perspective is determined by those two concepts which form the result: current operating concept and all inclusive concept. The first leads to the inclusion of the consequences of the operational activities in the profit-and-loss account, as being operations that permit the future performance of the enterprise to be seen, and the elements not related to the exploitation put emphasis on the owner's equity. Those who support the evaluation of performance in accordance with this approach tend to measure the performance of managers.

According to the second concept, all the elements which affect the growth or diminution in the owner's equity in a period, with the exception of the dividends suppliers or falls in capital through the distribution to the share holders or associates, lead to the measurement of the financial performance.

The two concepts have the function of providing for two types of user needs, one being the measurement of the activities' performance, current operating concept, and the other, the measurement of growth profit, in a patrimonial vision of the enterprise, all inclusive concept.

Performance is equal to the global result only if the global result does not take into account the pluses generated by the price rises of frozen assets used by the enterprise and in the same time, permits the maintenance of the entity's buying power.

The detailed expression that some authors propose for as complete as possible characterization of the enterprise's performance is:

Performance (global result) of the enterprise=

Profit/loss of the period acknowledged in the profit-and-loss account

+,- Income/expenses, gain/loss directly acknowledged in the owner's equity

+,- Profit/loss caused by effects of accounting politics modifications

+,- Profit/loss caused by effects of correction of fundamental errors.

The profit-and-loss account or the income account(profit and loss statement) is the synthesized accounting document which measures the performance of the enterprise's activity, in a given period of time: it constitutes a synthesis of flow accounting at a micro economical level.

The measurement of the enterprise's performances targets the profit's measurement, which can be approached from more than one perspective:

- patrimonial, by comparing the value of an enterprise at two different moments, using the same evaluation methods. The profit's measurement is made with the help of the following equation:

Assets- Liabilities= Owner's Equity

Owner's Equity afferent to exercise N- Owner's Equity afferent to exercise N-1= The result of exercise N

Fluctuation of owner's equity between two successive exercises- Increase in the social capital afferent to exercise N + Distribution of dividends and eventually reduction in the social capital afferent to exercise N= The result of exercise N.

- economic:

Income- Expenses= The result of the exercise

- financial:

Self-financing capacity- Expenses with depreciation and provisions= The result of the exercise

Economic activities and organizations that consume resources and produce results which generate modifications in the patrimony, are described and analyzed by the profit-and-loss account or the income account (profit and loss statement).

The use of economic means, resources and the generation of results are complex movements which give rise to transformations not only in the value, but also in the structure of the patrimony.

As a rule, income and expenses are not equal and as a consequence there is registered a modification in the volume of the patrimony.

In determining the result, the identification of the moment in which an activity of the enterprise ensues an expense or generates profit is essential. Expenses denote in expression (value) the patrimonial operations related to the acquisition and use of economic assets involved in the activity performed by the patrimonial unit.

The expenses of the entity represent the values paid or to be paid for:

- stock use, work and services rendered which benefit the entity

- employee's expenses

- the execution of legal and contractual obligations

In the exercise's expenses are also included the provisions, depreciation and adjustments for depreciation or the loss of patrimonial elements' value.

Income expresses the patrimonial relations regarding the wealth obtained from performed activity and from property owned[9]. Income of the exercise corresponds to an increase in the patrimonial assets (claims and liquid assets), and the exercise's expenses determine an increase in the patrimonial passive. In other words, income is perceived as a "source of wealth" which leads to the increase of the net statement, and expenses represent an "impoverishment" which determines a reduction in the net statement or a depreciation of assets. In the income category are included the amounts or values collected or to be collected in the owner's name from current activities, but also gains from other sources. If in the progress of a financial exercise, income is greater than expenses, the increase in patrimonial assets is bigger than the increase in the patrimonial passive, and the difference between these two represents the profit of the exercise, which in order for the patrimony to be balanced, is added to the owner's equity in passive. By comparing income and expenses it is determined the total result. The total result is presented in the form of profit if the income is greater than the expenses, and in the form of liability if the expenses exceed the income.

Demarcation and registration of expenses and income is made in accordance with the engagement criterion and not the collection or payment criterion. Expenses are registered in the moment when material goods are received or services rendered, and income is registered in the moment when material goods and services are obtained and sold.

3. Bibliography

Bernard Colasse (2005). *Comptabilité générale*. 9th Edition. Paris Economica Ph. H.

Emil Horomnea (2008). *The Scientific Basis Of Accounting. Doctrine. Concepts. Lexicon*. Iasi: Tipo Moldova Ph. H.

Jianu Iulia (2007). *The Evaluation, The Layout And The Analysis Of The Enterprise's Performance. An Approach From The Perspective Of The International Standards Of Financial Reporting*. Bucuresti: CECCAR Ph. H.

James Richard (1996). *Comptabilité et pratique comptable.* Paris: Dalloz PH. H.

Mihai Ristea; Oprea Calin (2002). *Principles of Accounting.* Bucuresti: Gemicod PH. H.

Judith Saghroun; Claude Simo. *Bilan ou compte de resultat Faut-il choisir*?. Nantes: Congrés AFC.

Jean Claude Scheid (1984). *La varieté des notions de résultat pour intreprinse*, Actes du 4-é Congres de l'AFC.

DEX (1996). Bucuresti: Univers Enciclopedic Ph. H.

[9] Mihai Ristea, Oprea Calin, "Principles of Accounting", Gemicod PH. H., Bucuresti, 2002, p. 84-85